STATE OF MICHIGAN
CIRCUIT COURT FOR THE 30TH JUDICIAL CIRCUIT
INGHAM COUNTY

E. L. COX, COMMISSIONER OF INSURANCE FOR THE STATE OF MICHIGAN,	
Petitioner,	
v	File No. 98-88265-CR
MICHIGAN HEALTH MAINTENANCE ORGANIZATION PLANS, INC., a Michigan health maintenance organization,	Hon. James R. Giddings A.G. No. 1998053333A
Respondent. _______________________________________/	

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COMMISSIONER'S PETITION FOR APPROVAL
OF PROPOSED FIRST AMENDED REHABILITATION PLAN

Frank Fitzgerald Commissioner of the Office of Financial and Insurance Services by Jennifer M. Granholm, Attorney General of the state of Michigan, and E. John Blanchard and Michael J. Fraleigh Assistant Attorneys General, move this Court for an Order that approves the proposed First Amended Rehabilitation Plan. In support of this Petition, the Commissioner relies on authority granted to him and the Court pursuant to MCL 500.8101 *et seq.* and in the facts and rationale set forth in this Petition and the proposed First Amended Rehabilitation Plan.

I.
STATEMENT OF FACTS

A. PROCEDURAL HISTORY

OmniCare Health Plan ("OmniCare") was placed under Supervision in 1998 as permitted under Chapter 81 of the Michigan Insurance Code, MCL 500.8100 *et seq*. due to its fiscal instability. In July 2001 the Commissioner, Office of Finance and Insurance Services of the State of Michigan (hereinafter, "Commissioner") petitioned the Court for an Order of Rehabilitation of OmniCare and the Court issued a Preliminary Order of Rehabilitation and Injunctive Relief. On September 11, 2001, the Court entered a final Order of Rehabilitation and Injunctive Relief. Under the Court's Order, the Commissioner is required to take such action, as he considers necessary or appropriate to reform or revitalize OmniCare and to pursue all avenues of reorganization, consolidation, conversion, merger, or other transformation so as to effectuate the rehabilitation and maintain a continuity of health care services. (Order of Rehabilitation, p. 3, September 11,2002). The Rehabilitation is currently being conducted in the interests of justice and for the protection of OmniCare's creditors, policyholders, and the public. MCL 500.8101(3).

Pursuant to MCL 500.8114, the Court appointed the Commissioner as the Rehabilitator. Commissioner Fitzgerald appointed Mr. Bobby Jones and Ms. Beverly Allen as Deputy Rehabilitators. Mr. Jones and Ms. Allen are responsible for the day-to-day operations of OmniCare.

In March 2002, the Commissioner submitted a proposed 2002 Rehabilitation Plan. The March 2002 Rehabilitation Plan's debt restructuring was based on the largest individual creditor receiving no cash and having its entire liability restructured into surplus notes. In order to implement the contemplated debt restructuring, an agreement on the terms of the surplus notes was required with the creditor, however, the creditor and the Commissioner were unable to reach an acceptable agreement. Accordingly, on May 23, 2002, the Commissioner advised the Court that he would submit a First Amended Rehabilitation Plan (hereinafter "Rehabilitation Plan").

B. SALIENT COMPONENTS OF THE REHABILITATION PLAN

Since Rehabilitation, OmniCare has had break-even or positive financial performance. In the last five (5) months of 2001, OmniCare generated a surplus of approximately $3.0 million. This positive financial performance has continued into 2002. OmniCare reported a surplus of approximately $700,000 for the first quarter of 2002. OmniCare is on target to hit its $3.4 million dollar surplus budgeted for 2002.

Other factors lend support to a successful turnaround for OmniCare. The creditor provider community has responded positively to discussions with the Deputy Rehabilitators for continuation of OmniCare. Creditor support is a result of significant improvements in OmniCare's operations since the Rehabilitation status, especially in the timely processing of claims to providers. Other operational improvements, to name a few, include improvements in capturing and reporting data to external sources, improvements in member and provider call response times and an increase in coordination of benefit savings.

Part of the financial improvement occurred as a result in the reduction of management fees that originally required OmniCare to pay a management company a fee of 17% of total operating revenues. This fee was later reduced to 14% in 1998. This percentage of revenue was originally intended to approximate administrative expenses. Since the Rehabilitation, OmniCare has been operating at an administrative cost approximating 10%, thereby generating a 4% savings to its bottom line.

If Liquidation is chosen for OmniCare instead of Rehabilitation, medical claims creditors would receive approximately $.26 on each dollar of debt. This would exhaust the funds available for distribution to creditors and would leave no money for other creditors. Conversely, the proposed Rehabilitation Plan provides, on a weighted average basis, medical claims creditors with approximately $.52 on each dollar of debt and allows partial payment of other claims.

In the Rehabilitation Plan, claims for medical services are stratified into eight categories: Subscribers, Physicians and Non-Physician Medical Providers, Individually Large Hospital Providers, Hospitals, Pay in Full Providers, Pharmacy, Primary Care Centers, Collection Agencies, and Primary Care Capitation Withhold Funds. This stratification is based on various criteria that include contractual rates of reimbursement, the ability of a creditor type to absorb write-offs and other factors set forth in the Rehabilitation Plan.

In the last seven months, OmniCare's improved performance has enabled it to increase its financial stability and improve its operational, medical, and quality metrics. These current trends lend themselves to a continued positive outlook for OmniCare's partners: employers, enrollees, contractors, providers, employees and the community-at-large.

II.
LAW AND ARGUMENT

A. THE COMMISSIONER IS AUTHORIZED TO DETERMINE THE BEST METHOD OF REFORMING OMNICARE, WHETHER THROUGH REHABILITATION OR LIQUIDATION

Under Michigan law, the Commissioner is authorized to "take such action as he or she considers necessary or appropriate to reform and revitalize the insurer." MCL 500.8114(2). The Commissioner has the sole discretion to determine how to reorganize or otherwise transform a financially troubled insurer. (Order of Rehabilitation, p.3, September 11, 2001) and MCL

500.8114(4). If the Commissioner determines that reorganization is appropriate, he is required to prepare a plan to implement the reorganization he deems necessary. Id. See also, *Foster v Mutual Fire, Marine & Inland Insurance Co*., 531 Pa 598, 608-609; 614 A2d 1086 (1992). A plan may include the equitable apportionment of any unavoidable losses. MCL 500.8101(3)(d).

In this case, the Commissioner has determined that Rehabilitation is the most appropriate method to reform and revitalize OmniCare as a financially stable insurer capable of continuing to provide managed care benefits to Medicaid recipients and commercial accounts. As required by statute, the Commissioner submits the Rehabilitation Plan to the Court for approval.

1. Rehabilitation is Preferred to Liquidation for a Financially Troubled Insurer

There is a strong public interest in favor of rehabilitation. In *State of Tennessee v. Xantus Healthplan of Tennessee*, 2000 WL 630858, p.11; 2000 Tenn. App. Lexis 319 (2000), the Tennessee Court of Appeals noted that rehabilitation is the preferred choice stating that:

> "Rehabilitation is preferred over Liquidation because of the public interest in insurance. *Minor v. Stephens*, 898 S.W.2d 71 (Ky.1995). Although the Commissioner may directly petition for liquidation without going through Rehabilitation, *United Physicians Ins. v. United American Bank of Memphis,* No. 01-A-01-9503-CH-00096 (Tenn.Ct.App. filed Feb. 7, 1996, in Nashville), the public interest generally favors Rehabilitation.

The Supreme Court of California noted this preference in *In re Executive Life Ins. Co.*, 38 Cal.Rptr.2d 453, 471-472 (Cal.App.1995):

> The public has a grave and important interest in preserving the business [of the insolvent insurer] if that is possible. Hence while the Commissioner as conservator has the power either to rehabilitate the insolvent insurer or to liquidate it, liquidation is a last resort. *Carpenter v. Pacific Mutual Life Ins. Co*., 10 Cal 2d 307 at 329, 74 P.2d 761 (1937).
>
> There appears from the pattern of the statutes dealing with insurer insolvencies an underlying theme of resolution of questions for the benefit of policyholders by Rehabilitation if possible. This is not merely a resolution of private rights, but also a matter of the public interest because of the character of insurance. (See *Carpenter v. Pacific Mut. Life Ins. Co., supra, 10 Cal. 2d 307, 329.)* In carrying out his or her responsibility, the Commissioner acts not only as a trustee but also as a servant of the state in the exercise of its police power. (See *Garris v. Carpenter (1939) 33 Cal. App. 2d*

> *649, 654-656 [92 P.2d 688].)* In some instances individual policyholders must suffer some detriment if this is necessary to carry out the purpose of the statutory scheme. (*Neblett v. Carpenter (1938) 305 U.S. 297, 305 [83 L. Ed. 182, 189, 59 S. Ct. 170].)* The limitation upon the Commissioner's authority is that its exercise be reasonably related to the public interest in rehabilitating the insurer (*Commercial Nat. Bank v. Superior Court, supra, 14 Cal. App. 4th at p. 416)* and not be arbitrary or improperly discriminatory. (*Carpenter v. Pacific Mut. Life Ins. Co., supra, 10 Cal. 2d at p. 335.)*.

Preserving the business of OmniCare is important for the State of Michigan to preserve a long-standing participant in providing the financing and delivery of health care to Medicaid and commercial members. The Rehabilitation Plan recognizes the failures of the past operation and has implemented new processes and procedures to financially improve the operations. Liquidation is not proposed by the Commissioner and should only be a last resort in the OmniCare matter.

B. <u>The Court is Required to Approve the Proposed Rehabilitation Plan if it is Fair and Equitable to all Parties Concerned.</u>

The Court is authorized to review the Commissioner's Rehabilitation Plan to determine whether it is "in the court's judgment fair and equitable to all parties concerned." MCL 500.8114(4). "All parties concerned" means OmniCare's policyholders, creditors, and the public. MCL 500.8101(3). After reviewing the Plan, and such hearings, as it deems necessary, the Court may:

(a) Approve the Plan;

(b) Disapprove the Plan; or

(c) Modify the Plan and approve it as modified.

MCL 500.8114(4). By statute, these are the Court's only choices.

A Rehabilitation Plan it is generally considered "fair and equitable" if the concerned parties will be better off under the Rehabilitation Plan than under a Liquidation of the insurer.

See, Grode v Mutual Fire, Marine & Inland Insurance Co, 132 Pa 196, 207; 572 A2d 798 (1989). In determining that the Rehabilitation Plan is fair and equitable to the concerned parties, this Court should take notice that:

- OmniCare's creditors will recover substantially more money on their claims under the rehabilitation than they would if OmniCare was liquidated.
- A Rehabilitation Plan is generally considered "fair and equitable" if the concerned parties will be better off under the Rehabilitation Plan than under a Liquidation of the insurer. *See, Grode v Mutual Fire, Marine & Inland Insurance Co*, 132 Pa 196, 207; 572 A2d 798 (1989).
- Since Rehabilitation, OmniCare has paid all of its debts as they become due and under the proposed Rehabilitation Plan, will continue to do so.
- OmniCare has dramatically increased its financial stability and net worth.
- Rehabilitation will preserve a long-standing participant in the financing and delivery of health care to Medicaid recipients.
- The Department of Community Health believes that OmniCare is "a critical player in the serving of our beneficiaries [Medicaid recipients] in this region [Southeastern Michigan]." Letter, James K. Haveman, Jr. to Honorable James R. Giddings, Judge of the Ingham County Circuit Court, p.1 (April 23, 2002).
- On April 30, 2002 the Department of Community Health renewed OmniCare's contract for another 2 years, until October 1, 2004, with the possibility of being extended for an additional year.

These factors are clear indications that the Rehabilitation Plan is fair and equitable to all parties concerned.

1. **The Court is required to Accord Great Deference to the Commissioner's Rehabilitation Plan.**

In reviewing the Rehabilitation Plan, the Court should be reminded that the Legislature has provided the Commissioner with discretion to determine the terms and conditions of a Rehabilitation Plan. The Court may note that this approach is consistent with the scope of review provided by the Courts in other States with statutes similar to MCL 500.8114. For example, in *Foster v. Mutual Fire, Marine & Inland Insurance Company*, 614 A.2d 1086, 1092-1093 (Pa.1992), the Court noted that:

> Numerous other jurisdictions in this country have also held that the decision of a Rehabilitator to rehabilitate the insolvent business of an insurer is within the sound discretion of the Rehabilitator and should not be rejected by the reviewing court unless the Rehabilitator has abused that discretion. *Kueckelhan v. Federal Old Line Insurance Co.,* 74 Wash.2d 304, 444 P.2d 667 (1968); *Carpenter v. Pacific Mutual Life Insurance Co.,* 10 Cal.2d 307, 74 P.2d 761 (1937), *aff'd sub nom. Neblett v. Carpenter,* 305 U.S. 297, 83 L.Ed. 182 (1938) . . .
>
> This Court has concluded that this great deference in favor of the Commissioner and the resulting narrow scope of review for the courts are in recognition of the expertise of the administrative agency or individual officer assigned the task of regulating a given industry. *See, e.g., Mathies Coal Co. v. Commonwealth, Department of Environmental Resources,* 522 Pa. 7, 559 A.2d 506 (1989); *Brocal Corporation v. Commonwealth, Department of Transportation,* 515 Pa. 224, 528 A.2d 114 (1987); *Pelton v. Commonwealth, Department of Public Welfare,* 514 Pa. 323, 523 A.2d 1104 (1987); *Pennsylvania Bankers Ass'n v. Secretary of Banking,* 481 Pa. 332, 392 A.2d 1319 (1978).

Furthermore, in *LaVecchia v. HIP of New Jersey, Inc*., 734 A.2d 361, 364 (N.J. Superior Court, 1999) stated:

> As Rehabilitator, the Commissioner has the discretion to determine the manner in which Rehabilitation will proceed and must submit a plan which is subject to approval, disapproval, or modification by the Court based upon its judgment as to what is fair and equitable to all parties concerned. *N.J.S.A. 17B:32-43(e)*. Thus, while the Commissioner's plan for Rehabilitation cannot be implemented without a Court finding that it is fair and equitable, deference is given to the means the Commissioner chooses to utilize in going forward with rehabilitation. As such, the Rehabilitator's determination concerning the manner in which to proceed will not be set aside unless it is shown to be arbitrary or unreasonable. *Fortunato v.*

> *New Jersey Life Ins. Co., 254 N.J. Super. 420, 603 A.2d 964 (App. Div. 1991).* Likewise, the Rehabilitator's decision to reject the plan submitted by HIPNJ is also entitled to deference and is not subject to review unless it is arbitrary or unreasonable.

Finally, support is also found in *Kueckelhan v Federal Old Line Insurance Co.*, 444 P2d 667, 673-674 (1968), where the Washington Supreme Court, in reviewing the trial court decision that rejected the Commissioner's rehabilitation plan in favor of the company's plan, stated:

> In this vein, and speaking of the part played by the court in a rehabilitation proceeding, we said in *Kueckelhan v. Federal Old Line Ins. Co. (Mutual), 69 Wn.2d 392, 418 P.2d 443 (1966),* at 406:
>
> > The court's sole and proper function in Rehabilitation proceedings is to direct -- that is, to supervise and review -- the actions of the Insurance Commissioner while he is operating the seized insurance company. The Courts cannot dictate or outline the general policy or course of conduct of the Insurance Commissioner or his department [Citing case.], because this outline is dependent on the terms of the applicable statutory provisions and not upon judicial discretion. Our statutory provisions, therefore, properly place the responsibility on both the Insurance Commissioner and the Courts, the Commissioner being required to follow the statutory mandates and to use reasonable discretion in the Rehabilitation of a seized company, with abuses of discretion to be checked by the judiciary. [Citing authority.]
> >
> > In this capacity, the Court is acting much in the same manner as it acts when overseeing a trust or probate; only in this instance, it is reviewing the Insurance Commissioner who is acting like a receiver or trustee and as an officer of the state. (Citing authority and case.) Moreover, the Insurance Commissioner is not acting as an agent of the courts. He holds his position as rehabilitator by force of legislative enactment, confirmed by court appointment. Consequently, the court's power of discretion, vis-a-vis the Insurance Commissioner, is curtailed by the Commissioner's statutory powers and the statutes governing the management of insurance companies and rehabilitation proceedings. [Citing authority.]
>
> This then is the role carried on by our courts under our laws relating to statutory Rehabilitation. The Court does not conduct the business of the seized company. This task is assigned by the legislature to the Insurance Commissioner

> who acts to protect the general public, the policyholders and owners of the company, and the company itself.

Accordingly, consistent with Michigan law, and the weight of authority, the Court should approve the Commissioner's Rehabilitation Plan. The Plan should not be rejected or modified unless the Court finds that the Plan:

(a) Is not fair and equitable to all parties concerned;

(b) Exceeds the Commissioner's statutory authority; or

(c) Constitutes an abuse of the Commissioner's statutory discretion.

2. <u>Dissatisfaction with the Debt Restructuring by Creditors is not a Basis to a Finding that the Plan is Unfair</u>.

It is crucial to review the Rehabilitation Plan therefore in its entirety. Analyzing statutory provisions similar to MCL 500.8114, the Michigan Supreme Court, in reviewing a Rehabilitation Plan for a bank, stated that:

> The final test is that the Court before which the proceeding is pending may order the stockholders and depositors to accept and abide by any such plan of reorganization which 'shall be fair and equitable under all the circumstances of the case. *State Banking Commissioner v Peoples Wayne County Bank of Hamtramck (On Application For Rehearing)*, 296 Mich 330, 342 (1941).

Not all of OmniCare's creditors are content with the proposed Rehabilitation Plan. Naturally, they would like to recover 100% of their prerehabilitation claims. Objections by individual creditors as to the amounts each will receive under the Rehabilitation Plan is not the proper subject of inquiry for this Court because a finding as to the fairness to each individual creditor will not further the legislative intent of MCL 500.8101 *et. seq*.. Rather, the Rehabilitation Plan must be considered in its totality when the Court determines whether it is fair and equitable. As noted in *Vickodil v Commonwealth of Pennsylvania*, Insurance Dept., 126 PA Commonwealth Ct 390, 397; 559 A2d 1010 (1989):

> [I]ndividual interests may have to be compromised in order to avoid greater harm to a broader spectrum of policyholders and the public.

In *Foster*, *supra*, several objections by creditors were filed against the entry of an order approving a Rehabilitation Plan in Pennsylvania. There the Court readily acknowledged that in order to foster the goals of Rehabilitation, the Rehabilitator must be given power to manage and control existing liabilities in order to reorganize and stabilize the financial structure of the troubled insurer. The Court stated, at. 1100, that:

> While perfection may be an unattainable characteristic of the Plan, this does not provide us with legitimate grounds for disturbing the more expert approval of provisions, which are manifestly reasonable. So long as the provisions of the Plan strike a fair and proper balance between the competing secured and unsecured creditors the Plan must survive the objections raised to it.

The court also noted that while the effect of the plan may cause economic suffering to some private contracting parties, some individual interests may be compromised in order to preserve the ultimate goal of rehabilitation. *Id*. at 1094.

The Rehabilitation Plan has been designed to provide the greatest relief possible to OmniCare's creditors while protecting the interests of its members and the public. The Rehabilitation Plan is fair and equitable to OmniCare's creditors, members and the public. Accordingly, the Rehabilitation Plan should be approved.

RELIEF REQUESTED

Based on the forgoing, the Commissioner requests that the Court enter an order that:

1. Approves the form and substance of the Rehabilitation Plan;
2. Authorizes the Commissioner to implement the Rehabilitation Plan;
3. Restructures OmniCare's debt as set forth in the Rehabilitation Plan;

4. Requires payment to OmniCare's creditors as set forth in the Rehabilitation Plan;

5. Discharges and releases OmniCare from all of its prerehabilitation debts, liabilities and claims against it except as provided for in the Rehabilitation Plan;

6. Allows the restructuring and transformation of OmniCare as contemplated in the Rehabilitation Plan; and

7. Provides such other and further direction as may be necessary to fully implement and effectuate the Rehabilitation Plan.

Respectfully submitted

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